

**Statement of
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Deputy United States Trade Representative
before the
Committee on Transportation & Infrastructure
Subcommittee on Aviation
United States House of Representatives
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Chairman Mica, Mr. Costello, and Members of the Subcommittee, I am pleased to have the opportunity to appear before you today to testify on the U.S. jet transport industry and global market factors and policies affecting U.S. producers. I am going to focus today on a particular global factor affecting U.S. producers – subsidies for the development and production of large civil aircraft – and on the Administration’s ongoing efforts to end subsidies to the European aircraft manufacturer, Airbus.

I will begin today with some historical background on the subsidy issue and on past U.S. efforts to address EU aircraft subsidies. I will then discuss developments over the past year, as the Administration, in close cooperation with the U.S. industry, intensified its efforts to end the subsidization of Airbus. I will then turn to the current situation and our plans for going forward.

The Subsidization of Airbus

Mr. Chairman, Airbus was established in 1970 as a European consortium of French, German, and later, Spanish and U.K. companies. It formally became a single integrated company in 2001. Airbus is 20 percent owned by BAE Systems of the U.K., and 80 percent owned by the European Aeronautic Defence and Space Company ("EADS"). EADS itself is 15 percent owned by the French State, and 5 percent owned by Spain.

Over its 35-year history, Airbus has benefited from massive amounts of EU Member State and EU subsidies that have enabled the company to create a full product line of aircraft and gain more than a 50 percent share of large civil aircraft ("LCA") sales. Every major Airbus aircraft

model was financed, in whole or in part, with government subsidies taking the form of "launch aid" – financing with no or low rates of interest, and repayment tied to, and entirely dependent on, sales of the financed aircraft. If sales of a particular model are below an agreed number, Airbus does not have to repay the financing. EU governments have forgiven Airbus debt; provided equity infusions; provided dedicated infrastructure support; and provided substantial amounts of research and development funds benefiting civil aircraft projects.

Since 1985, the United States has been involved in several rounds of negotiations with the Airbus partner governments and the European Commission, with the objective of achieving greater disciplines over the subsidies provided to Airbus. In 1989 and 1991 the United States brought two cases at the GATT challenging Airbus subsidies. The first case challenged a German program that offset adverse exchange rate fluctuations on sales of Airbus aircraft, and the second, broader case challenged overall subsidies to Airbus. The first case ended in a victory for the United States after a GATT panel determined that the exchange rate scheme constituted a prohibited export subsidy. The EU blocked adoption of the panel report, which was permitted before the creation of the WTO, but Germany subsequently withdrew the scheme.

The United States withdrew the second case in July 1992 after the two sides negotiated a bilateral agreement limiting government support for large civil aircraft programs. The agreement included a prohibition of future production support and a limitation on the share of government support for the development of new aircraft programs to 33 percent of a project's total development costs.

Three years later, the WTO Subsidies Agreement entered into force. The agreement applies in full to subsidies for large civil aircraft. Therefore, if a Member provides a subsidy that is inconsistent with the agreement's terms, it is subject to challenge at the WTO.

Despite these obligations, the EU has continued to subsidize Airbus. The \$3.7 billion in launch aid that EU governments committed for the Airbus A380 "super jumbo" was the largest amount

of funds committed for a single project. The EU provided further loans and infrastructure that pushed the total amount of A380 subsidies to approximately \$6.5 billion. Airbus is on the verge of launching another new aircraft, the A350, and it has requested \$1.7 billion in risk-free launch aid for that aircraft as well, even though it has stated publicly that it could “easily” finance the project itself. Of course, even if it could easily finance the project, a risk-free advance of \$1.7 billion provides a very significant competitive advantage over Boeing, its U.S. competitor, which has to bear the risk of launching new models without the support of the U.S. Treasury.

Efforts to Negotiate a New Bilateral Agreement

Mr. Chairman, our current effort to end the subsidization of Airbus began early last year, when it became apparent that EU Member States were considering subsidies for the A350. U.S. and EU officials had extensive conversations in the late spring and early summer, and two sets of meetings in July and then again in September, as the United States sought an EU agreement to negotiate an end to subsidies. President Bush instructed USTR to pursue all options to end the subsidization of Airbus, including the filing of a WTO case, if need be. The U.S. industry fully supported this approach.

Unfortunately, the EU was not willing to agree to the goal of ending new subsidies, much less on how to achieve this goal. Therefore, on October 6, 2004, we initiated the first stage of dispute settlement proceedings at the WTO by requesting consultations with the EU. The EU responded by requesting consultations on alleged U.S. subsidies to Boeing. We also exercised our right to terminate the 1992 Agreement at that time.

Although we held WTO consultations with the EU in November, we were unable to resolve our concerns. Then, on January 11, 2005, when we were on the verge of moving to the next stage of our WTO challenge, we reached agreement with the EU on a framework for negotiating an end to subsidies. We agreed with the EU to set a 90-day time frame for the negotiations. The agreement included a common goal of ending subsidies, as defined by the WTO Subsidies

Agreement. The agreement applied equally to the United States and the EU. We appreciate the support of the U.S. industry and the Congress during that period of negotiation.

In March, EU officials introduced a new set of conditions for the negotiations and backed away from the agreed objective of ending subsidies. They appear to have changed their position because certain EU Member States want to continue providing launch aid subsidies to Airbus, in particular for the Airbus A350.

The EU argues that it needs to continue providing launch aid to offset subsidies that Boeing allegedly receives from NASA and the Department of Defense. There is no basis for the EU's claim. We don't agree that NASA and Defense contracts provide subsidies to Boeing. But in any event, Airbus and its parents, EADS and BAE Systems, have space and defense businesses that rival Boeing's. Therefore, even under the EU's unfounded approach, Airbus benefits as much if not more than Boeing.

In addition, while the EU criticizes Boeing for receiving U.S. defense contracts, BAE Systems is one of the Defense Department's top ten contractors. It is involved in billions of dollars worth of Pentagon contracts, including the Joint Strike Fighter. EADS is currently seeking incentives from U.S. states to locate a new aerial refueling tanker facility in the United States. It plans to manufacture the tankers by converting Airbus large civil aircraft, the development of which, of course, has been subsidized.

Furthermore, Airbus has received billions of euros in subsidies from the EU Member States for infrastructure and for civil aerospace R&D. For example, when Airbus Germany needed to expand its production facilities for the Airbus A380, the Hamburg government spent 750 million euros to fill in a protected wetland. Similarly, the French government spent 180 million euros to create an aerospace industrial park where Airbus is assembling the A380. The European Investment Bank also underwrites Airbus's programs, including a 700 million euro loan to EADS to help underwrite the costs of developing the A380.

Meanwhile, the European Commission R&D “Framework” programs are devoting ever increasing amounts of funds to aerospace R&D. The European Commission “Sixth Framework” program alone granted 1.1 billion euros to aerospace projects. The research programs at the EC level are also supplemented by R&D programs at the national level that provide even more funds to Airbus. Unlike in the United States, the EC research often takes the form of direct cash grants to Airbus, and it focuses on projects with outcomes that can be applied commercially to products in the near- and medium-term.

It is clear that Airbus and Boeing are both active players in the defense and space markets, and that both companies receive contracts for R&D. But only Airbus receives launch aid. There is no similar type of financing available in the United States.

Launch aid is a particularly distortive type of subsidy because it shifts the enormous up-front expense and commercial risk of developing new aircraft from Airbus to European taxpayers. EU governments help underwrite new Airbus aircraft programs, and if Airbus guesses wrong about the market for a particular aircraft, it does not need to repay the money.

Moreover, because repayment is tied to sales, Airbus receives a substantial grace period before it needs to begin repayment. For example, Airbus has not even begun repaying the \$3.7 billion that it received for the A380. Nevertheless, EU governments are preparing to give it even more money for the A350.

Launch aid also frees up funds that Airbus would normally need to invest in developing its new aircraft programs so that it can use the money for other purposes. For example, in March, at the same time that Airbus was asking for \$1.7 billion in launch aid for developing the A350, its parent company BAE Systems spent \$4 billion to purchase the U.S. manufacturer of the Bradley Fighting Vehicle.

The EU's continuing use of launch aid is also spawning imitators. On May 13th, the Canadian government announced that the Federal government and the Province of Quebec would provide launch aid to the Canadian firm Bombardier to help underwrite the costs of developing its new "C-Series" aircraft. Interestingly, the UK government also announced that it would provide launch aid to underwrite the Bombardier project. All told, these governments have committed \$700 million to Bombardier. With 110-135 seats, the proposed Bombardier aircraft will compete directly with Boeing and Airbus aircraft for the first time.

Current U.S. Efforts to End Subsidies

Mr. Chairman, the Administration continues to believe that a negotiated outcome that ends launch aid and other WTO-incompatible subsidies would be the preferred route for resolving this matter. But let me be clear. If we conclude that a negotiated solution to end subsidies is not possible in the near term, we will return promptly to the WTO. We believe we have a very strong case, and we are prepared to move forward. The Administration is committed to ending the subsidization of Airbus and establishing a level playing field for trade in large civil aircraft. Ambassador Portman, the recently-confirmed U.S. Trade Representative, already has spoken several times with his European counterpart, EU Trade Commissioner Peter Mandelson, on this subject. He has been crystal-clear in describing the U.S. position. It is up to the Europeans to decide if they are prepared to withhold launch aid while negotiating an agreement, or if they'd rather take their chances in a WTO dispute proceeding.

We look forward to working with you, the members of this subcommittee and other interested members of Congress, and with the U.S. industry, to stop the unfair subsidization of Airbus.

Thank you.